STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of **MICHIGAN CONSOLIDATED GAS COMPANY** for authority to increase its rates and for other relief.	)	Case No. U-13898
In the matter of the application of **MICHIGAN CONSOLIDATED GAS COMPANY** for approval of depreciation accrual rates and other related matters.	)	Case No. U-13899

At the July 19, 2005 meeting of the Michigan Public Service Commission in Lansing, Michigan.

PRESENT: Hon. J. Peter Lark, Chairman
Hon. Laura Chappelle, Commissioner
Hon. Monica Martinez, Commissioner

ORDER GRANTING REQUEST FOR REHEARING IN PART

On April 28, 2005, the Commission issued its order in these combined dockets (April 28 order), which granted Michigan Consolidated Gas Company (Mich Con) an increase in annual gas revenues of $60,756,000 and authorized new depreciation accrual rates for the company. On May 27, 2005, Mich Con filed a request for rehearing and clarification of the April 28 order. On June 7, 2005, the Commission Staff (Staff) filed its response to the request for rehearing and clarification. On June 17, 2005, the Association of Businesses Advocating Tariff Equity (ABATE) and Attorney General Michael A. Cox (Attorney General) filed responses to the request for rehearing and clarification.

In the April 28 order, the Commission reviewed the testimony, exhibits, and arguments of the parties. The Commission found, among other things, that certain costs and expenses presented by Mich Con were not appropriate for inclusion in the 2005 test year. Mich Con disagrees with certain of the Commission's determinations. In the company's request for rehearing and clarification, Mich Con argues that the Commission's determinations are incorrect or improper regarding six items: 1) the company's disposition of the Guardian Building[1] (and the eventual loss on the sale of that building) as well as the usefulness of 90% of the company's former Customer Information System (CIS);[2] 2) recovery of the premium paid by DTE to purchase the stock of MCN; 3) the non-executive employee incentive plan; 4) revisions to Mich Con's depreciation rates; 5) safety and training-related operation and maintenance (O&M) expenses; and 6) the rate established for off-system transportation, Rate TOS-F and Rate TOS-I.

ABATE, the Attorney General, and the Staff argue that rehearing is not appropriate.[3] In their view, the April 28 order has considered all of the arguments that are now re-presented by Mich Con in its request for rehearing and clarification. Accordingly, they argue, the company has not met the Commission's requirements for rehearing of the April 28 order.

Discussion

Rule 403 of the Commission's Rules of Practice and Procedure, 1999 AC, R 460.17403, provides that a petition for rehearing may be based on claims of error, newly discovered evidence,

[1]Prior to the merger of MCN Energy Group, Inc. (MCN), and DTE Energy Company (DTE), the Guardian Building was the corporate headquarters for MCN and also for its principal subsidiary, Mich Con. Discussion of the Guardian Building includes the First Street Parking Deck, which was available to those employees working at the Guardian Building.

[2]The CIS is a client server-based computer system designed to integrate all customer service business functions through use of a Windows™-based information management system tied to all customer accounts by customer name. *See,* the June 2, 1998 order in Case No. U-11669.

[3]The Staff would revise the off-system transportation rate as requested by Mich Con.

facts or circumstances arising after the hearing, or unintended consequences resulting from compliance with the order. A petition for rehearing is not merely another opportunity for a party to argue a position or to express disagreement with the Commission's decision. Unless a party can show the decision to be incorrect or improper because of errors, newly discovered evidence, or unintended consequences of the decision, the Commission will not grant a rehearing.

<u>The Guardian Building and the CIS</u>

In the April 28 order, the Commission found that neither the Guardian Building nor 90% of the CIS was used and useful in providing utility service. In Mich Con’s view, the April 28 order is in error because the use of these assets in utility service is not the deciding factor. Rather, the company argues, if the initial purchase of those assets was a prudent action, then recovery of the total cost of the assets over time must be permitted regardless of their disposition or continued use in utility service. Further, the company states, the impact of the merger of MCN and DTE on the usefulness of the assets in utility service has no bearing on cost recovery of those assets. In Mich Con’s view, the purchase of both the Guardian Building and the CIS were prudent actions and recovery from ratepayers of all of the costs related to those assets must be allowed.

Moreover, Mich Con states, because 90% of the CIS was found not used and useful, Statement of Financial Accounting Standard (FAS) No. 144 required the company to immediately write down the asset to reflect that determination. This non-recurring accounting adjustment affected the company’s earnings before interest, taxes, depreciation, and amortization (EBITDA) ratio for the first quarter of 2005. Because of this, the company states, it was not able to comply with EBITDA debt covenants for certain of its credit facilities. However, Mich Con continues, the lenders associated with those credit facilities waived compliance with the EBITDA ratio covenants for the first quarter of 2005, which allowed the company to remain in compliance with all of its

debt covenants. In the company's view, it is reversible error for the Commission to place Mich Con in a position where it would breach a debt covenant. Mich Con argues that the Commission must provide the company sufficient funds to avoid that situation and thus should revise the April 28 order accordingly.

ABATE states that the Guardian Building and 90% of the CIS are not used and useful in providing utility service and those related costs should not be reflected in Mich Con's rates. ABATE notes that a utility may only earn a return on property that is used and useful in providing service to the utility's customers, and that if property is not so used and useful, then the company may not earn a return on that property. ABATE states that the Commission's disallowance of those costs was proper and, consequently, rehearing on this issue is inappropriate.

The Staff states that, except for the triggering of EBITDA ratio covenants in two short-term debt agreements, Mich Con has not raised new arguments regarding the Guardian Building and the CIS. The Staff notes that Mich Con's lenders have waived compliance with the EBITDA ratio covenants, and there is no reason to expect that the lenders will change their minds, given that Mich Con's financial position will improve because of the additional rate relief granted to the company by the April 28 order. For these reasons, the Staff argues, Mich Con has not met the standard of Rule 403 and a grant of rehearing on this issue is not appropriate.

The Commission agrees with ABATE and with the Staff. The issues raised by Mich Con have been reviewed and decided in the April 28 order. Moreover, Mich Con's lenders have waived compliance with the debt covenants that it presents as a reason to rehear the April 28 order. The non-compliance with certain debt covenants was created by a convergence of factors, including the non-recurring adjustments that caused the situation—as explained in footnote 5 to Mich Con's request for rehearing and clarification. Such conditions are not likely to recur and should be eased

by the added revenues provided by the April 28 order. Thus, the one new issue raised by Mich Con has been resolved and cannot support its request for rehearing. Accordingly, the Commission finds that Mich Con has not met the requirements of Rule 403 and rehearing will not be granted on this issue.

The over-market premium paid by DTE to acquire MCN

The April 28 order did not allow recovery of the over-market premium paid by DTE to acquire control of MCN, the "control premium." Mich Con states that the synergies of the DTE/MCN merger are inherent within all of the company operational cost data presented for the 2005 test year. Thus, the company argues, it is improper to set rates based upon the combined operation of DTE/MCN without allowing recovery of the control premium paid by DTE for MCN. In the company's view, Mich Con's ratepayers now enjoy all of the benefits that the merger created, but those same ratepayers do not bear any of the substantial costs incurred to create those benefits.

Additionally, Mich Con argues, the Staff's tax-loss adjustment to the absolute amount of the control premium was improper. In the company's view, the value of all of the MCN tax losses was reflected in the market value of MCN at the time of the merger; DTE's eventual use of those tax losses to offset other DTE income is immaterial to recovery from Mich Con's ratepayers of the full value represented by those tax losses. The company further disagrees with the Staff's position regarding amortization of the control premium. The company acknowledges that FAS 141 and FAS 142 eliminated the requirement for annual amortization of any goodwill balance, and that those standards now require a yearly review to determine if impairment charges should be taken. However, in the company's view, a 40-year amortization of the DTE/MCN control premium will provide a more predicable annual amount than would the annual impairment review. Thus, the

company argues, the Commission should reverse the April 28 order, and provide for the 40-year amortization of the DTE/MCN control premium and its full rate recovery.

ABATE states that Mich Con's petition for rehearing relating to the control premium issue contains no new argument, nor any other material, that has not already been presented to the Commission. ABATE argues that Mich Con is merely re-arguing its prior position, and that, consequently, rehearing should not be granted on this issue. ABATE states that it and other parties presented significant evidence that contradicted Mich Con's assertions of synergy savings from the merger of DTE and MCN. ABATE argues that only net benefits from the merger were appropriate for review. In ABATE's view, the Commission correctly reviewed the entire record and properly determined that a net benefit did not accrue to Mich Con's ratepayers from the merger of DTE and MCN. Accordingly, ABATE argues, it was proper to exclude the control premium when calculating 2005 test year expenses.

The Attorney General notes that Mich Con does not make reference to newly discovered evidence or unintended consequences regarding the control premium issue. Rather, the Attorney General states, Mich Con simply re-argues its position and states that the Commission's April 28 decision is unreasonable. The Attorney General argues that Mich Con simply believes that the company's position on the control premium issue is more reasonable than the other positions presented, and that the Commission was wrong when it failed to accept Mich Con's position in the April 28 order. Consequently, the Attorney General states, Mich Con does not meet the rehearing requirements of Rule 403.

The Staff states, simply, that Mich Con presents no arguments on the control premium issue that were not previously considered, and rejected, by the Commission. Accordingly, the Staff states that rehearing on this issue is not appropriate.

The Commission has reviewed Mich Con's request for rehearing regarding the control premium issue. As argued by ABATE, the Attorney General, and the Staff, Mich Con does not raise new issues; the company simply expresses disagreement with the Commission's decision and re-presents arguments that it has previously made. Because of this, the Commission finds that Mich Con has not met the Rule 403 requirements regarding this issue and rehearing will not be granted.

The non-executive employee incentive plan

Mich Con argues that the Commission's April 28 decision regarding the company's non-executive employee incentive plan was unjustified. In the company's view, Administrative Law Judge Mark E. Cummins (ALJ) determined to allow 50% of the cost of the non-executive employee incentive plan, and the Commission erred when it adopted the Attorney General's position to exclude 100% of that plan's cost. In Mich Con's view, the company must have a two-component pay system—base pay and incentive pay—to attract and to retain a skilled workforce, and the total compensation package for its employees that Mich Con presented to the Commission was reasonable; thus, that entire compensation package should have been allowed. Moreover, the company states, the Commission has misinterpreted its decision in Cases Nos. U-10149 and U-10150; it argues that decision provides no precedent for non-executive compensation plans.

ABATE notes that the Commission's decision in Cases Nos. U-10149 and U-10150 did deal with an executive bonus program, but that the decision also indicated that any similar type of incentive program would require a showing that benefits to ratepayers would be commensurate with the cost of the program. ABATE states that Mich Con simply failed to provide the necessary showing to support each of its incentive plans. ABATE argues that Mich Con has shown no error,

new information, or unintended consequence from the Commission's decision on this issue and, thus, rehearing is not appropriate.

The Attorney General states that, beyond merely presenting evidence in support of the company's incentive plans, Mich Con bore the burden of proof on the issue of employee incentives. In the Attorney General's view, Mich Con did not meet that burden of proof, and the Commission appropriately adopted the Attorney General's position on executive bonuses and non-executive employee incentive compensation. The Attorney General states that Mich Con's arguments on rehearing of this issue are the same arguments that the company raised in its exceptions to the proposal for decision (PFD) in this proceeding, and that the company presented in its testimony and briefs to the ALJ. Thus, the Attorney General argues, rehearing should not be granted.

The Staff states that the April 28 order treated the executive bonus plan and the non-executive employee compensation plan separately—contrary to Mich Con's assertion that the order denied recovery of non-executive employee incentive amounts based on precedent applicable only to executive bonuses. In the Staff's view, the Commission found, and explicitly stated, that the evidence presented by Mich Con regarding executive bonuses did not meet the standard of Cases Nos. U-10149 and U-10150, and the Commission also separately found appropriate the Attorney General's position regarding the recovery of non-executive employee incentive plan costs. Accordingly, the Staff argues, rehearing is inappropriate because the Commission correctly applied the Cases Nos. U-10149 and U-10150 standard regarding executive bonuses and properly accepted the Attorney General's position regarding the non-executive employees incentive plan.

The Commission has reviewed Mich Con's argument, and does not agree that the standard established in Cases Nos. U-10149 and U-10150 was improperly applied in the April 28 order. As

stated by the Staff, the Commission found that the executive bonus expenses proposed by Mich Con did not meet the standard established in Cases Nos. U-10149 and U-10150, and the Commission separately found that the Attorney General's position regarding non-executive employee compensation was appropriate. Thus, Mich Con's argument supporting its request for rehearing is incorrect, and the company fails to meet the Rule 403 standard. Because of this, rehearing will not be granted.

Revised depreciation rates

Mich Con argues that the Commission misapprehends the order it issued in Case No. U-14292, which established a generic proceeding to review depreciation practices for Commission-jurisdictional entities. In the company's view, the Commission's order establishing Case No. U-14292 precludes any revision to Mich Con's depreciation rates until the conclusion of that case. The company disagrees with the Commission's statements to the contrary in its April 28 order, and restates the arguments presented in Mich Con's exceptions to the PFD. In the company's view, any of the various Commission determinations that may occur in the generic proceeding may affect Mich Con's depreciation accrual rates. Consequently, the company argues, because of the possible effects of that generic case, any change in Mich Con's depreciation rates prior to the final conclusion of Case No. U-14292 would be unlawful and improper.

ABATE states that Mich Con does not present a valid legal argument as to why revised depreciation rates cannot be adopted in this proceeding. In ABATE's view, the depreciation case, Case No. U-13899, was properly noticed and then properly consolidated with the rate case; thus, all depreciation issues were properly before the Commission for its review and determination. ABATE argues that Mich Con's revised depreciation accrual rates are based on record evidence in this proceeding and were set using the Commission's broad rate-making authority. While ABATE

acknowledges that the generic Case No. U-14292 may (or may not) have an effect on Mich Con's future depreciation accrual rates, ABATE argues that in a case specifically noticed to review depreciation rates, it was appropriate for the Commission to establish revised just and reasonable depreciation accrual rates based upon the record evidence after finding that the existing rates were not reasonable.

The Attorney General states that Mich Con's argument regarding the effect of the generic Case No. U-14292 was previously argued by Mich Con in its exceptions to the PFD and then specifically addressed by the Commission in its April 28 order. Thus, the Attorney General argues, the change in depreciation rates cannot be an unintended consequence of the April 28 order, the Rule 403 standard has not been met by Mich Con, and rehearing on this issue is inappropriate.

The Commission has reviewed Mich Con's argument regarding the preclusive effect of the Commission's October 14, 2004 order in Case No. U-14292. The Commission addressed that argument in the April 28 order. While Mich Con alleges that the April 28 order is in error regarding this issue, the Commission does not agree. Mich Con has not presented new argument, new evidence, or unintended consequences flowing from the April 28 order regarding this issue. Accordingly, the Commission finds that Mich Con has not met the Rule 403 standard and rehearing will not be granted on this issue.

<u>Increased safety and training-related expenses</u>

In its April 28 order, the Commission allowed as a test-year expense an additional $6.9 million of safety and training-related O&M expenses above the Staff's $17.8 million historically based test-year projection. However, because that amount was above the historically based test-year projection, the excess amount was granted subject to refund if the increased amount was not

expended by Mich Con on safety and training-related areas.[4] An annual report of safety and training-related expenditures must be filed along with the company's annual filing concerning its Uncollectible Expense True-up Mechanism (UETM). The company now states that the safety and training-related O&M expenses included by the Commission within the test year (both historically based and additional) have as a cost-component the non-executive employee incentive compensation that the Commission determined should be excluded from the test year. Mich Con states that this occurs because the safety and training-related O&M expenses contain substantial amounts of labor expense—which of necessity included the incentive compensation. In Mich Con's view, it is improper to include such costs in the safety and training-related O&M expense while disallowing the same costs elsewhere. Accordingly, Mich Con requests that the Commission reduce the amount authorized for safety and training-related O&M expenses subject to refund by $1.465 million, which represents the incentive pay component of non-executive employee wages included within the test year's entire safety and training-related O&M expense.

The Attorney General argues that the effect of the disallowance of non-executive employee incentive compensation upon the remaining components of the test year is not an unintended consequence of the April 28 order. Rather, the Attorney General states, many of the Commission's rulings in the April 28 order require the company to recalculate and reduce other items as a result of the interlocking nature of the issues in a rate case. In the Attorney General's view, such recalculations and reductions are a normal product of a rate proceeding, are insufficient to support a rehearing request, and the Commission should deny rehearing on this issue.

The Staff argues that Mich Con's request is inappropriate. As the Staff views Mich Con's request, the company acknowledges that its rate relief included $24.7 million for safety and

[4] *See*, the April 28, 2005 opinion and order in Cases Nos. U-13898 and U-13899, page 74.

training-related items, but that the company would now only be required to expend $23.2 million on these safety and training items because of the incentive-related labor cost issue—in effect retaining the remainder for other uses within the utility. The Staff argues that a refund mechanism is already in place for any unexpended safety and training-related amounts, and, accordingly, rehearing is unnecessary—any amount not spent on the appropriate safety or training items can be refunded to Mich Con's ratepayers.

The Commission has reviewed Mich Con's argument and does not agree that clarification or rehearing is necessary for this issue. Safety and training-related O&M expenses comprise a number of general categories within the supporting documentation of this proceeding. The refund mechanism becomes operative only when, in total, the authorized amount has not been expended on the many safety and training-related areas presented in the company's testimony. The annual report that must be filed along with the UETM filing will allow the Commission to determine if the total amount was expended on safety and training-related items. Accordingly, the Commission finds that Mich Con has not met the Rule 403 standards on this issue and rehearing will not be granted.

Off system transportation rates TOS-F and TOS-I

Lastly, Mich Con states that the off-system transportation rates approved for rate schedules TOS-F and TOS-I are incorrect. The approved rates are those originally filed by Mich Con. However, the company states that the cost of service finally authorized in this proceeding differed from that originally filed and, thus, the TOS-F and TOS-I rates should have been revised in the final order. The company computes a revised rate for rate schedules TOS-F and TOS-I of $0.02120 per 100 cubic feet. The Staff supports Mich Con's request, and the remaining parties did not contest this revision.

The Commission has reviewed the computation presented by Mich Con and the underlying record and exhibits. The Commission agrees that the TOS-F and TOS-I rates were improperly calculated and grants rehearing on this limited issue. The Commission finds that the authorized rate for rate schedules TOS-F and TOS-I should be revised to $0.02120 per 100 cubic feet.

The Commission FINDS that:

a. Jurisdiction is pursuant to 1909 PA 106, as amended, MCL 460.551 *et seq.*; 1919 PA 419, as amended, MCL 460.51 *et seq.*; 1939 PA 3, as amended, MCL 460.1 *et seq.*; 1969 PA 306, as amended, MCL 24.201 *et seq.*; and the Commission's Rules of Practice and Procedure, as amended, 1999 AC, R 460.17101 *et seq.*

b. The off-system transportation rates approved for rate schedules TOS-F and TOS-I in the April 28 order should be revised as provided in Attachment A.

c. In all other aspects, Mich Con has not met the standards for rehearing that are contained within Rule 403, and rehearing should not be granted.

THEREFORE, IT IS ORDERED that:

A. The off-system transportation rates approved for rate schedules TOS-F and TOS-I in the April 28, 2005 order in this proceeding are revised as provided within Attachment A.

B. In all other respects, the petition for rehearing filed by Michigan Consolidated Gas Company on May 27, 2005 in this proceeding is denied.

C. Within 30 days, Michigan Consolidated Gas Company shall file revised rate schedules and tariffs reflecting the rates and tariffs approved in this order and shown in Attachment A.

The Commission reserves jurisdiction and may issue further orders as necessary.

Any party desiring to appeal this order must do so in the appropriate court within 30 days after issuance and notice of this order, pursuant to MCL 462.26.

MICHIGAN PUBLIC SERVICE COMMISSION

/s/ J. Peter Lark
Chairman

(S E A L)

/s/ Laura Chappelle
Commissioner

/s/ Monica Martinez
Commissioner

By its action of July 19, 2005.

/s/ Mary Jo Kunkle
Its Executive Secretary

The Commission reserves jurisdiction and may issue further orders as necessary.

Any party desiring to appeal this order must do so in the appropriate court within 30 days after issuance and notice of this order, pursuant to MCL 462.26.

MICHIGAN PUBLIC SERVICE COMMISSION

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Chairman

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Commissioner

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Commissioner

By its action of July 19, 2005.

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Its Executive Secretary

(Continued From Sheet No. F-18.00)

Rate Schedule TOS-F (Continued) **Applicable to all Districts**

Imbalance:

Company and Customer shall work to keep the gas flow in balance at all times. If at any time, the volumes of gas received by Company at the Receipt Point(s) are greater or lesser than the gas delivered at the Delivery Point(s), Company may refuse, increase or decrease deliveries to correct the imbalances. If, upon termination of a Contract, Customer has not delivered to Company quantities of gas that are equal to those Customer has taken at the Delivery Point(s), Customer must deliver the deficient volumes to Company, within 60 days of the termination of Contract, at a mutually agreeable rate of delivery. If Customer fails to correct the imbalance within the 60 day period, then Customer shall pay an unauthorized usage charge to Company at a rate of the highest price reported for MichCon, Michigan, Consumers Energy and Chicago LDCs during the applicable Month as reported by Gas Daily or, in the event that Gas Daily discontinues its reporting of such prices, any comparable reporting service, plus $1.00 per 100 cubic feet for all gas taken by Customer in excess of the cumulative volume delivered to Company (less use and loss) on behalf of Customer.

Gas in Kind

Company shall retain 1.42% of all gas received at the Receipt Point(s) to compensate it for the allowance for company-use and lost-and-unaccounted-for gas on Company's system. This volume shall not be included in the quantity available for delivery to Customer. In no event will Customer pay Gas-in-Kind more than once on the same volumes.

Rates:

(a) For contracts less than 365 days, a rate as mutually agreed to by Customer and Company and set forth in Contract, consisting of a demand portion and/or a commodity portion.

(b) For contracts equal to or exceeding 365 days, a rate not to exceed **$0.02120** per 100 cubic feet, consisting of a demand portion and/or a commodity portion shall be mutually agreed to by Customer and Company and set forth in Contract.

Late Payment Charge and Due Date

A late payment charge of 2% shall be applied to the unpaid balance outstanding if the bill is not paid in full on or before the date on which the bill is due. The due date of the customer's bill shall be 21 days from the date of mailing.

(Continued From Sheet No. F-20.00)

Rate Schedule TOS-I (Continued) **Applicable to all Districts**

Imbalance:

Company and Customer shall work to keep the gas flow in balance at all times. If at any time, the volumes of gas received by Company at the Receipt Point(s) are greater or lesser than the gas delivered at the Delivery Point(s), Company may refuse, increase or decrease deliveries to correct the imbalances. If, upon termination of a Contract, Customer has not delivered to Company quantities of gas that are equal to those Customer has taken at the Delivery Point(s), Customer must deliver the deficient volumes to Company, within 60 days of the termination of Contract, at a mutually agreeable rate of delivery. If Customer fails to correct the imbalance within the 60 day period, then Customer shall pay an unauthorized usage charge to Company at a rate of the highest price reported for MichCon, Michigan, Consumers Energy and Chicago LDCs during the applicable Month as reported by Gas Daily or, in the event that Gas Daily discontinues its reporting of such prices, any comparable reporting service, plus $1.00 per 100 cubic feet for all gas taken by Customer in excess of the cumulative volume delivered to Company (less use and loss) on behalf of Customer.

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